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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268–0001

INSTITUTIONAL COST CONTRIBUTION REQUIREMENT FOR COMPETITIVE PRODUCTS	Docket No. RM2012-3

REPLY COMMENTS OF THE UNITED STATES POSTAL SERVICE
(May 7, 2012)

Initial comments have been submitted in this docket by William C. Miller, the Parcel Shippers Association (PSA), the Public Representative, United Parcel Service (UPS), and the United States Postal Service. The Postal Service hereby provides its reply comments. The Postal Service focuses largely on the comments of UPS.

I. *Maintenance of Established Commission Method*

In Docket No. RM2007-1, the Postal Regulatory Commission made two determinations as to 39 U.S.C. § 3633(a)(3): first, it determined that the best method for implementing the section 3633(a)(3) contribution requirement was to require that competitive products cover a specified share of institutional costs; and second, it determined that the specified share should be 5.5 percent. In its initial comments, UPS advises the Commission to revisit the first determination and choose a new method for implementing the statutory requirement. UPS makes two arguments to support its position, the first of which is well encapsulated in the following excerpt:

> The rapid and substantial decline in First-Class Mail volume and revenue, the growth in competitive revenue from increased e-commerce goods delivery and the substantial, ongoing transfers of formerly market-dominant products to the competitive category all combine to undercut the current approach. Under that approach, competitive products need not make any additional contribution to institutional costs, even though

> additional contribution from competitive products could help ease the Postal Service's financial issues.[1]

In making this argument, UPS conflates the issue of whether the current method best reflects the section 3633(a)(3) directive with the separate, distinct issue of whether the current institutional cost share level of 5.5 percent is appropriate. All of UPS's points go to the second issue, not to the first. Even if is true that competitive products constitute a growing share of the Postal Service's offerings, it does not follow that the Commission's method is flawed.

UPS's second argument for replacing the current method is that the method cannot adapt quickly enough to changing realities:

> The current approach also fosters substantial regulatory lag: there may be no change in competitive products' required contribution to reflect any of these (or other) changes to the competitive products grouping until the next appropriate share review.[2]

The Commission addressed this specific concern in a previous ruling in this docket:

> The PAEA, however, specifically authorizes the Commission to revise its competitive product rules "from time to time." 39 U.S.C. 3633(a). Thus, the Commission is not limited to reviewing competitive products' contribution at 5 year intervals. The Commission's ability to conduct reviews more frequently than every 5 years is key to providing parties and the Commission with an appropriate mechanism to deal with relevant circumstances that may cause the Commission to change its rule regarding the minimum required contribution to institutional costs for competitive products.[3]

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[1] Initial Comments of United Parcel Service on Notice of Proposed Rulemaking to Evaluate the Institutional Cost Contribution Requirement for Competitive Products, Docket No. RM2012-3 (Apr. 9, 2012) ("UPS Comments"), at 7.
[2] *Id.* at 8. The particular changes that UPS is referring to here are transfers of products from the market dominant list to the competitive list.
[3] Order No. 1276, Order Granting, In Part, Motion of the Parcel Shippers Association to Extend the Period for Comments, Docket No. RM2012-3 (Mar. 7, 2012), at 4.

Thus, if circumstances change such that the Commission's current method is no longer the best method for implementing section 3633(a)(3), the Commission can change the method.[4]

A final flaw in UPS's position is that UPS barely explores any viable alternative. UPS devotes exactly one sentence to alternatives:

> For example, the appropriate share could be based on a cost or burden approach, such as equal cost coverages (a similar institutional cost allocation approach was proposed during the development of PAEA), or on a market-based approach, such as percentage share of revenue.[5]

Replacing a well-established method that the Commission adopted explicitly because "it better reflects the section 3633(a)(3) directive and is more easily understood than the various alternatives" should require a more compelling showing than the sentence above.[6]

II. *Other Issues*

Notwithstanding UPS's stated position, one might interpret the points it raises – particularly the points regarding the growth experienced by the Postal Service's competitive products and the fact of products being transferred to the competitive list – as counseling an increase of the specified share of institutional costs to be covered by competitive products above 5.5 percent. In response, the Postal Service would reiterate its explanation from its initial comments as to why the 5.5 percent level should be retained. In brief, the institutional cost share requirement is, as the Commission has

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[4] Further, in regard to the example posited by UPS, namely product transfers, 39 C.F.R. § 3020.32(c) ensures that product transfer proceedings consider the effect of transfers on compliance with section 3633(a)(3).
[5] UPS Comments, at 10.
[6] Order No. 26, Order Proposing Regulations to Establish a System of Ratemaking, Docket No. RM2007-1 (Aug. 15, 2007), at ¶ 3050.

recognized, a floor, not a target.[7] The floor should be neither so low as to give the Postal Service an artificial competitive advantage, nor so high as to constrain the Postal Service's flexibility. The market share evidence presented by the Postal Service demonstrates that the floor is not too low, while the circumstantial evidence noted in the Postal Service's initial comments indicates that the floor is too high. Nonetheless, given the fact that the Postal Service has transferred some products to the competitive list, and given other considerations, the Commission should maintain 5.5 percent as the specified share but give itself the authority to determine, on a case-by-case basis, that contribution below 5.5 percent of institutional costs is statutorily "appropriate," based on the circumstances obtaining at the time of any shortfall.

The Public Representative and PSA also counsel the Commission to maintain the specified share at 5.5 percent. While the Postal Service agrees with them, it believes that the explanation above is a stronger and more apt basis for reaching the parties' shared conclusion, rather than the future uncertainty that PSA and the Public Representative largely rely on. In addition, the Postal Service agrees in a general sense with William C. Miller that, because the Postal Service aims to maximize contribution from competitive products, the appropriate share requirement is functionally unnecessary. But the Postal Service nonetheless believes that the requirement serves a purpose by assuring other parties that the Postal Service will not shift away from its contribution-maximizing approach.

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[7] *See id.* at ¶ 3056 (stating that the requirement "is a floor for all competitive products, but the hope (and expectation) is that competitive products will generate contributions in excess of the floor").

Respectfully submitted,

UNITED STATES POSTAL SERVICE

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